

Message Text

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TO AMEMBASSY CAIRO

C O N F I D E N T I A L STATE 045385

FOR UNDER SECRETARY ROBINSON

FOLLOWING REPEAT ALGIERS 467 ACTION SECSTATE INFO LONDON
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QUOTE

C O N F I D E N T I A L ALGIERS 0467

DEPARTMENT PASS EXIMBANK

NAIROBI FOR UNDER SECRETARY ROBINSON

E.O. 11652: GDS

TAGS: EFIN AG

SUBJEQT: ALGERIAN FINANCIAL SITUATION: SIGNS OF STRAIN

1. SUMMARY: ALGERIA IS REACHING A TURNING POINT IN ITS DEVELOPMENT PROGRAM. THUS FAR IN ITS FOUR-YEAR PLAN, THE COUNTRY HAS USED FUTURE OIL AND GAS REVENUES AS COLLATERAL FOR ITS BORROWING AND IN 1975 BORROWED OVER \$3 BILLION FOR DEVELOPMENT. IN THE FIRST SEVEN MONTHS OF 1976, ALGERIA PLANS TO BORROW MORE THAN \$1.8 BILLION. SIGNS OF FINANCIAL STRAIN, HOWEVER, ARE SHOWING, AND THE ALREADY TIGHT FINANCIAL SITUATION MAY BE AGGRAVATED BY MILITARY EXPENDITURES IN CONNECTION WITH THE SPANISH SAHARA PROBLEM. WHILE
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ALGERIA IS LIKELY TO BE SUCCESSFUL AGAIN IN 1976 IN BORROWING SIGNIFICANT AMOUNTS, ITS ABILITY TO BORROW AT THIS PACE IN 1977 IS DOUBTFUL. FURTHER, MUCH OF THIS YEAR'S CAPITAL IMPORTS ARE BEING DEVOTED TO LNG PROJECTS,

MEANING THAT INCREASING DELAYS IN NON-LNG DEVELOPMENT PROJECTS CAN BE EXPECTED. END SUMMARY.

2. BACKGROUND. ALGERIA'S FOUR-YEAR DEVELOPMENT PLAN IS NOW AT ITS HALF-WAY POINT. DURING THE FIRST TWO YEARS OF THE PLAN, ALGERIA HAS VASTLY ACCELERATED ITS DEVELOPMENT EFFORT TO TAKE ADVANTAGE OF ITS MUCH INCREASED REVENUES FROM OIL. DOZENS OF INDUSTRIAL PROJECTS HAVE BEEN STARTED DURING THIS PERIOD. MANY MORE PROJECTS, HOWEVER, ARE NOW REACHING THE CONTRACT NEGOTIATING STAGE. THESE INCLUDE STEEL AND ELECTRICAL COMPLEXES, TRAINING CENTERS, MARITIME FLEET EXPANSION PROGRAMS, ALUMINUM PLANT, GAS HANDLING FACILITIES, AND A HOST OF OTHERS, MANY COSTING HUNDREDS OF MILLIONS OF DOLLARS. LARGELY BECAUSE OF THESE PAST AND PRESENT DEVELOPMENT EFFORTS, THE DEGREE OF EXTERNAL BORROWING HAS RISEN RAPIDLY TO THE POINT WHERE ALGERIA IS SPENDING 15 PERCENT OF ITS FOREIGN EXCHANGE REVENUE TO SERVICE A DEBT WHICH IS NOW ESTIMATED TO BE ABOUT \$7 BILLION. FINANCING HAS BECOME THE KEY ELEMENT IN ALL NEW CONTRACT NEGOTIATIONS TO THE EXTENT THAT PRIORITIES ARE NO LONGER BEING SET BY GOA DEVELOPMENT PLANNERS, BUT BY THE GENERAL FINANCIAL SITUATION, AND THE AVAILABILITY OF CREDIT FOR SPECIFIC DEVELOPMENT PROJECTS.

3. BORROWING SITUATION. IN 1975, ALGERIA RAN A TRADE DEFICIT VARIOUSLY ESTIMATED AT BETWEEN \$800 MILLION AND OVER \$2 BILLION. TO THE ALGERIANS, THIS HAS MEANT AN INCREASING NEED TO BORROW TO MAINTAIN THE PLANNED PACE OF DEVELOPMENT. ALTHOUGH COMPLETE INFORMATION IS NOT AVAILABLE ON ALGERIA'S BORROWING ACTIVITIES, THE FOLLOWING IS INFORMATION AVAILABLE TO EMBASSY ON RECENT AND PLANNED BORROWING BY THE GOA AND ITS BANKS:

A. SINCE SEPTEMBER OF 1975 THE ALGERIANS HAVE BORROWED OR RECEIVED COMMITMENTS FOR:

- \$400 MILLION FROM THE EURODOLLAR MARKET FOR GENERAL PURPOSES.
- \$330 MILLION FROM BELGIUM FOR LNG
- \$450 MILLION FROM SPAIN FOR LNG AND OTHER USES

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-(4;3#MILLION FROM THE IBRD FOR VARIOUS PROJECTS
(ACCORDING TO WORLD BANK FIGURES, ALGERIA BORROWED ON A COMMITMENT BASIS \$3.3 BILLION FROM EXTERNAL SOURCES IN 1975. WE UN-AWARE OF EXACT COMPOSITION OF THIS AMOUNT.)

B. AT PRESENT THE GOA HAS THE FOLLOWING DEFINITE BORROWING PLANS:

- SONATRACH IS FINALIZING PLANS FOR A \$400-\$500 MILLION EURODOLLAR LOAN FROM SYNDICATE MANAGED BY BANK OF AMERICA. ISSUE SHOULD BE PLACED ON THE MARKET WEEK OF FEB 23.
- SONATRACH IS DISCUSSING WITH U.S. EXIMBANK BORROWING OF

ADDITIONAL FUNDS FOR COMPLETION OF ARZEW-1 LNG PROJECT.
ADDITIONAL FINANCING NEEDS HAVE BEEN ESTIMATED AT
\$100-\$200 MILLION.

- SONELEC WILL SEEK \$50 MILLION IN U.S. FINANCING FOR
GTE HOME ELECTRONICS PROJECT, AS SOON AS MARKET IS
RECEPTIVE, PROBABLY IN MAY OF THIS YEAR.

- SONATRACH IS INHGBAFWIP Q QNLMF# NEGOTIATIONS WITH JAPAN
EXIMBANK CONCERNING \$450 MILLION CREDIT FOR PURCHASE OF
GAS TREATMENT FACILITIES TO BE LOCATED AT HASSI R'MTB.
FACILITIES WILL BE SUPPLIED BY JAPAN GASOLINE CO.

- SONATRACH IS DISCUSSING WITH THE ECGD, THE BRITISH EXIMBANK
BANK, THE APPLICATION OF \$200 MILLION LINE OF CREDIT,
WHICH APPARENTLY IS STILL CURRENT, TO THE CONSTRUCTION
COSTS OF THE ARZEW II LNG PROJECT.

THE ABOVE DEFINITELY PLANNED BORROWING PROJECTS TOTAL IN THE
RANGE OF \$1.3 BILLION.

C. OVER THE NEXT SEVERAL MONTHS, THE GOA HAS THE FOLLOWING
OTHER BORROWING PLANS:

- THE EXTERNAL BANK OF ALGERIA (BEA) NOW HAS IN FINAL
STAGE PLAN FOR \$200 MILLION EURODOLLAR LOAN FOR
EXPANSION OF ALGERIAN MARITIME FLEET. DETAILED PLANS
EXIST FOR PURCHASE OF NINETEEN ADDITIONAL SHIPS,
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LARGE MAJORITY OF WHICH ARE USED VESSELS. AT SAME
TIME, ALGERIANS HOPE TO FINANCE PURCHASE OF SEVERAL
THOUSAND CONTAINERS. MANUFACTURERS HANOVER TRUST IS
NOW DISCUSSING MANAGING THIS ISSUE FOR THE ALGERIANS.

- SONATRACH WILL NEED SUBSTANTIAL ADDITIONAL FINANCING FOR
CONSTRUCTION OF RECENTLY SIGNED ARZEW-II CONTRACT.
DEPENDING ON HOW MUCH OF CURRENT EURODOLLAR ISSUE IS
APPLIED TO PROJECT, AS MUCH AS \$350 MILLION IN
SUPPLIERS CREDIT WILL HAVE TO BE LOCATED IN THE NEXT
SIX MONTHS FOR NECESSARY EQUIPMENT.

THIS COULD BRING TOTAL PROBABLY BORROWING IN THE NEXT SIX OR
SEVEN MONTHS TO \$1850 MILLION.

4. MEANWHILE, THE REST OF ALGERIA'S DEVELOPMENT PROGRAM NEEDS
CONTINUE, GENERATING ADDITIONAL FINANCING REQUIREMENTS. WE HAVE
NO WAY OF CALCULATING THE AMOUNT OF SUPPLIERS CREDITS WHICH
ALGERIANS WILL SEEK FROM VARIOUS COUNTRIES FOR SUCH THINGS AS
DIJEL STEEL MILL COMPLEX, GAS PIPELINES, ALUMINUM PLANT, TEXTILE
FACILITIES, ETC. IN ADDITION, WE UNDERSTAND FROM U.S. BANKING
SOURCES THAT ALGERIAN MISSION OF "SENIOR ECONOMISTS" PLAN TO
VISIT NEW YORK IN MARCH OR APRIL TO DISCUSS POSSIBILITY OF MARKET-

ING ALGERIAN BONDS ON U.S. FIXED RATE MARKET.

5. GIVEN THIS VORACIOUS FINANCING PROGRAM, IT IS NOT SURPRISING THAT ALGERIANS FIND THEMSELVES AT THE MOMENT IN A CASH FLOW SHORTAGE SITUATION. EVIDENCE OF THIS CASH BIND IS BECOMING MORE AND MORE EVIDENT:

A. POSITIONS IN U.S. BANKS ARE WEAKER. ALGERIANS HAVE RECENTLY WITHDRAWN COVER FOR LETTERS OF CREDIT IN SEVERAL U.S. BANKS. AT MOMENT, WHEN BANKS ARE REQUIRED TO MAKE PAYMENTS UNDER LETTER OF CREDIT, THEY MUST WIRE ALGERIAN BANKS FOR PAYMENT. ONE ALGERIAN BANK, THE CREDIT POPULAIRE D'ALGERIE HAS BEEN IN OVERDRAFT POSITION WITH PHILADELPHIA NATIONAL BANK FOR MORE THAN NINETY DAYS.

B. FINANCIAL PROBLEMS MAY HAVE CONTRIBUTED TO THE DEPARTURE OF FINANCE MINISTER MAHROUG. MAHROUG HAD REPORTEDLY TRIED EVERY TRICK HE KNEW TO REDUCE SPENDING AND EXPAND REVENUES. NEW TAXES ON VEHICLES IMPORTED BY ALGERIAN OVERSEAS WORKERS, HOWEVER, HAD PROVEN UNPOPULAR. MAHROUG'S EFFORTS TO SYSTEMITIZE AND LIMIT CONFIDENTIAL

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EXTERNAL BORROWING BY ALGERIAN NATIONAL COMPANIES HAD ALSO APPARENTLY MET WITH LITTLE SUCCESS. IN ADDITION, BECAUSE OF CURRENT POLITICAL SITUATION WITH MOROCCO, SAUDI ARABIA AND KUWAIT HAD REPORTEDLY WITHDRAWN EARLIER PLEDGES OF \$500 MILLION IN CREDITS PROMISED LAST FALL.

C. MINIERAL BARTER ARRANGEMENTS ARE BEING INCREASINGLY PUSHED. ALGERIAN NATIONAL COMPANIES ARE ASKING FOREIGN SUPPLIERS TO ACCEPT PARTIAL OR TOTAL PAYMENT FOR PRODUCTS IN COMMODITY TERMS. DURING RECENT TEXTILE NEGOTIATIONS WITH U.S. CONSORTIUM, AMATEX, ALGERIANS ASKED GROUP TO ACCEPT DOWN PAYMENT EITHER IN FORM OF IRON ORE OR IN PHOSPHATES.

MORE STRIKING CASE WAS THAT OF HUGHES TOOLS WHICH LAST YEAR PROVIDED ALGERIA WITH 60 PERCENT OF THE ROCK BITS USED IN OIL DRILLING. HUGHES NOW TALKING TO ALGERIANS ABOUT \$20 MILLION CONTRACT TO FURNISH BITS FOR FUTURE DRILLING PROGRAMS. HUGHES FIRST ASKED TO TAKE 100 PERCENT OF COST OF BITS IN FORM OF PHOSPHATE OR IRON ORE. AFTER NEGOTIATION, IT WAS AGREED THAT HUGHES WOULD TRY TO LOCATE BUYER FOR ALGERIAN MINERALS WORTH HALF OF CONTRACT VALUE. HUGHES REPS WERE NOT SANGUINE ABOUT EASE OF LOCATING SUCH BUYERS. THIS COMPENSATORY FINANCING EFFORT, ACCORDING TO ONE MINISTRY OF INDUSTRY AND ENERGY OFFICIAL APPLIES TO CERTAIN EXTENT TO ALMOST ALL DEVELOPMENT PROJECT ON WHICH FINANCING WILL BE SOUGHT IN 1976.

D. INDUSTRIAL PROJECTS ARE BEING POSTPONED. BEA OFFICIAL RECENTLY TOLD U.S. BANKER THAT THOUGHT BEING GIVEN TO EXTENDING FOUR-YEAR PLAN BY ONE YEAR. THOUGH SUCH AN ACTION IS FAR FROM DEFINITE, IT DOES INDICATE THAT THERE ARE DELAYS IN DEVELOPMENT PLAN. RE INDICATIONS AVAILABLE TO THE EMBASSY, A U.S. BUSINESSMAN WAS RECENTLY TOLD THAT FURTHER WORK ON MOSTAGANEM

PAPER PLANT WAS BEING DELAYED BECAUSE OF POLITICAL SITUATION; A GE REP SAYS HIS COMPANY LOSING CONFIDENCE THAT "ALGERIANS SERIOUSLY INTERESTED (OR ABLE) TO BEGIN WORK ON GENERATING FACILITIES FOR DJIJEL STEEL PROJECT; AND SWEDISH EMBASSY REPORTS THAT FOUR OF PROJECTS IN WHICH SWEDISH COMPANIES INTERESTED HAVE BEEN POSTPONED; FRENCH BUSINESSMAN REPORTS THAT WILAYA AUTHORITIES WHO PREVIOUSLY PAID FOR SMALL CONTRACTS (\$1-2 MILLION) IN CASH ARE NOW ASKING FOR CREDITS AND THAT TWO LARGE PROJECTS GOA PREVIOUSLY PUSHING HARD ON HAVE LAPSED INTO STAGE OF DESULTORY DISCUSSIONS.

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E. NEW CONTRACTS DEPEND ON FINANCING. FINANCE IS "THE" KEY QUESTION OF IMPORTANCE IN ANY CONTRACT NEGOTIATION UNDERTAKEN BY ALGERIAN NATIONAL COMPANIES THESE DAYS.

6. TO A CERTAIN EXTENT, ALGERIAN DEFENSE EXPENDITURES MAY ALSO BE CONTRIBUTING TO THE CURRENT FINANCIAL CRUNCH. ALGERIANS' MILITARY EFFORT RELATED TO SAHARA PROBLEM IS DIVERTING EQUIPMENT AND PRESUMABLY FINANCIAL RESOURCES FROM DEVELOPMENT. ONE MINISTRY OF INDUSTRY AND ENERGY SOURCE RECENTLY TOLD EMBOFF THAT SAHARA SITUATION WAS DIRECTLY RESPONSIBLE FOR COMPENSATORY FINANCING (BARTER) SCHEME MENTIONED ABOVE. MORE BROADLY, HOWEVER, THE ALGERIAN FINANCIAL PICTURE WAS STRETCHED BEFORE THE SPANISH SAHARA SITUATION BEGAN. THE CURRENT IMBROGLIO HAS ONLY MANAGED TO TIGHTEN THE AVAILABILITY OF FOREIGN EXCHANGE A LITTLE BIT MORE.

7. THE CONCLUSION FROM ALL THESE BITS AND PIECES ON THE ALGERIAN FINANCIAL SCENE IS THAT ALGERIA IS PASSING OUT OF THE PHASE OF ABUNDANT CAPITAL AVAILABILITY WHICH CHARACTERIZED THE TWO YEARS AFTER THE JUMP IN THE PRICE OF CRUDE OIL. DURING THE FIRST TWO YEARS OF THE 1974-1977 DEVELOPMENT PLAN, INTEGRATED AND COORDINATED DEVELOPMENT HAS BEEN THE CONCEPT. NO PROJECT THAT FIT INTO THIS TOTAL DEVELOPMENT CONCEPT HAS BEEN TOO EXPENSIVE OR TOO ADVANCED TO CONSIDER. THE TIMES ARE CHANGING, HOWEVER, AT THE MOMENT, THE ALGERIANS ARE DOING THEIR BEST TO PUSH BACK THE INEVITABLE CUTBACK OF THE DEVELOPMENT PLAN WITH AMBITIOUS BORROWING SCHEMES. AT THE SAME TIME, HOWEVER, UNEXPECTED CASH OUTLAYS FOR MILITARY ITEMS ARE PUSHING IN THE OTHER DIRECTION.

8. FROM ALL INDICATIONS AVAILABLE TO EMBASSY, ALGERIANS CAN CONTINUE TO BORROW IN THE U.S. AND ON THE EURODOLLAR MARKET AT A SUBSTANTIAL PACE FOR THE NEAR TERM. FOR THIS YEAR, THE INFLOW OF CAPITAL IS LIKELY TO CONTINUE AT A HIGH RATE. OUR STRONG IMPRESSION IS THAT THE INTERNATIONAL BANKING COMMUNITY CONTINUES TO HAVE CONFIDENCE IN ALGERIA'S ABILITY TO REPAY ITS DEBTS. 1977, HOWEVER, MAY BRING THE NEAR SATURATION OF THE WESTERN FINANCIAL MARKET WITH ALGERIAN PAPER MEANING A REDUCTION IN THE RATE OF INFLOW OF FOREIGN BANK CAPITAL. (IF THE BORROWING RATE IS STEPPED UP, SATURATION WILL OF COURSE COME SOONER.)

IN THIS EVENT, THERE WILL BE MANY PROJECTS IN THE PLAN
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THAT WILL NOT BE COMPLETED. FURTHER,
IF THE OVERRIDING PRIORITY IN FOREIGN BORROWING CONTINUES TO BE
GIVEN TO LNG DEVELOPMENT (AND PERHAPS OCEAN TRANSPORTATION) AS IS
NOW THE CASE, MORE DELAYS IN NON-LNG PROJECTS CAN BE EXPECTED IN
THIS YEAR.

9. THE EMBASSY BELIEVES THAT A SLOWDOWN IN DEVELOPMENT MAY WELL
TURN OUT TO BE IN THE LONG TERM BEST INTERESTS OF ALGERIA. THE
PACE OF DEVELOPMENT IN THE LAST TWO YEARS HAS BEEN TOO RAPID.
THERE ARE MANY HALF FINISHED DEVELOPMENT PROJECTS IN THE COUNTRY
THAT HAVE RUN INTO ONE OBSTACLE OR ANOTHER, AND MANY OTHER
PLANTS THAT HAVE OPERATING DIFFICULTIES THAT LIMIT OUTPUT
TO LOW PERCENTAGES OF CAPACITY. KEY DECISION MAKERS, HOWEVER,
HAVE NOT HAD ENOUGH TIME TO DEVOTE TO SUCH PROBLEMS WHEN THEY
ARE IN THE MIDST OF NEGOTIATING HUNDRED MILLION DOLLAR CONTRACTS.
A TIME TO DIGEST IS CLEARLY NEEDED.
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